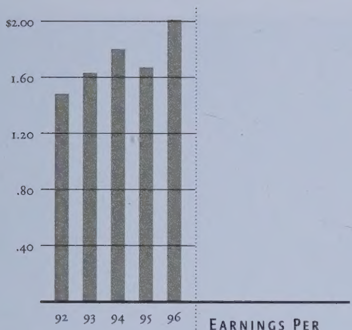
PACIFIC NORTHERN GAS LTD. *Annual Report 1996*

Corridor for Growth

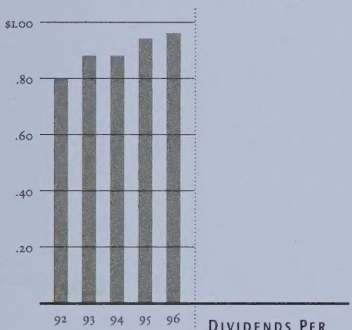
Vision Statement

Pacific Northern Gas will be a customer-focused and market-driven company. We will be competitive by providing service of superior value to our customers. Our key success factors will be safety, reliability, low cost, operating efficiency and adherence to high environmental standards. ☐ We will achieve our vision by fully utilizing the skills and abilities of our employees to provide sustained value to all customer groups and to meet our commitments to other stakeholders. ☐ Pacific Northern Gas will align the interests of its shareholders, employees and customers to create significant business value characterized by excellent financial results, outstanding professional accomplishments and superior performance.

Business Highlights



Earnings Per Common Share



Dividends Per Common Share

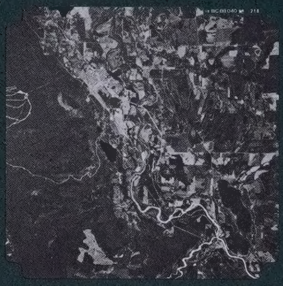
□ Pacific Northern's net income in 1996 was $7.39 million, 19 percent greater than the net income of $6.19 million reported in 1995. □ After providing for preferred share dividends, earnings per common share in 1996 were $2.01 compared with $1.67 in 1995. Dividends paid to common shareholders were 96 cents per share, up two cents from the preceding year. □ A record 1,340 customers were added to the system during 1996. At year end the Company was providing service to some 28,000 customers. □ Pacific Northern acquired Centra Gas Victoria Inc. The acquisition will enable utilization of certain non-capital tax losses with an estimated current value of $1.6 million □ Agreements were reached concerning the acquisitions of Centra Gas Fort St. John Inc. The acquisitions will add some 8,000 accounts to the Company's customer base. □ Additions to property, plant and equipment totalled $9.8 million, compared with $14.3 million in 1995. □ Natural gas deliveries during the year totalled 38.7 petajoules, 11.7 percent greater than in 1995 and 0.7 petajoules greater than the previous record in 1994. □ Gas sales to off-system customers totalled 0.8 petajoules. The decline from the 2.1 petajoules recorded in 1995 is primarily attributable to strong demand from the Company's own customers as well as commencement of the use of underground gas storage.

Comparative Financial Highlights

Years ended December 31	1996	1995	1994	1993	1992
Total energy delivered (TJ)	**38 716**	34 656	38 026	37 506	34 096
Net income (000)	**$ 7,385**	$ 6,191	$ 6,601	$ 5,963	$ 5,403
Earnings per common share*	**2.01**	1.67	1.80	1.63	1.48
Dividends per common share*	**0.96**	0.94	0.88	0.88	0.80
Total investment in utility plant (000)	**168,493**	165,149	156,593	146,090	127,640

* *Adjusted to reflect the August 20, 1993 split of Class A Common Shares and Class B Common Shares on a two-for-one basis.*

Terrace



Smithers / Telkwa

Fort St. John

Prince Rupert

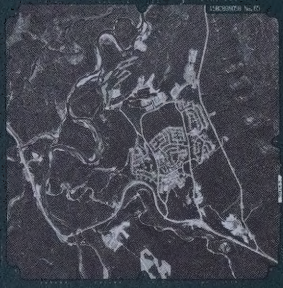
Khyex / Skeena confluence

Dawson Creek

Corridor for Growth

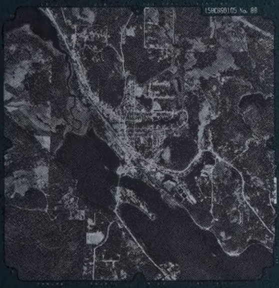
Along a corridor of rivers, highways, railways, natural gas and electric lines lie these 14 communities. It is a corridor endowed with a bounty of natural resources. Forests, fish, arable land, minerals, hydrocarbons and water resources each contribute to the corridor's success. □ The corridor's production and shipment of commodities add substantially to the provincial and national economies. Meeting demands in an international marketplace are chemicals, refined metals, metal concentrates, coal, pulp, lumber and food products. Expanded production and value added processing are anticipated in the years ahead, along with a diversification of business activity to meet the growing local demand. □ The corridor's future will be enhanced by the attractive lifestyle it offers. Its residents enjoy an increasingly broad range of commercial products and services. The healthy, outdoor-oriented environment offers diverse recreational opportunities. Ready access to educational and medical facilities, affordable housing and a strong sense of neighbourhood add to the incentive to reside within the corridor. □ Pacific Northern Gas looks forward to its ongoing role as a key supplier of energy products and services to support the corridor's growth.

Fort St. James



Tumbler Ridge

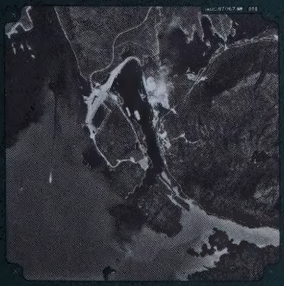
Pouce Coupe



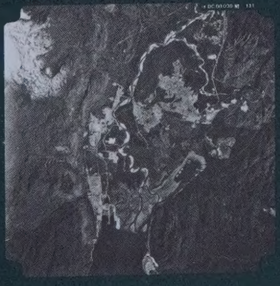
Burns Lake

Fraser Lake

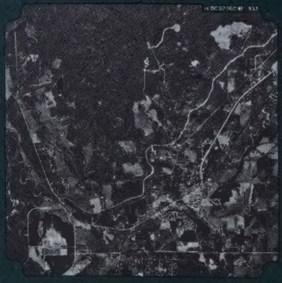
Vanderhoof



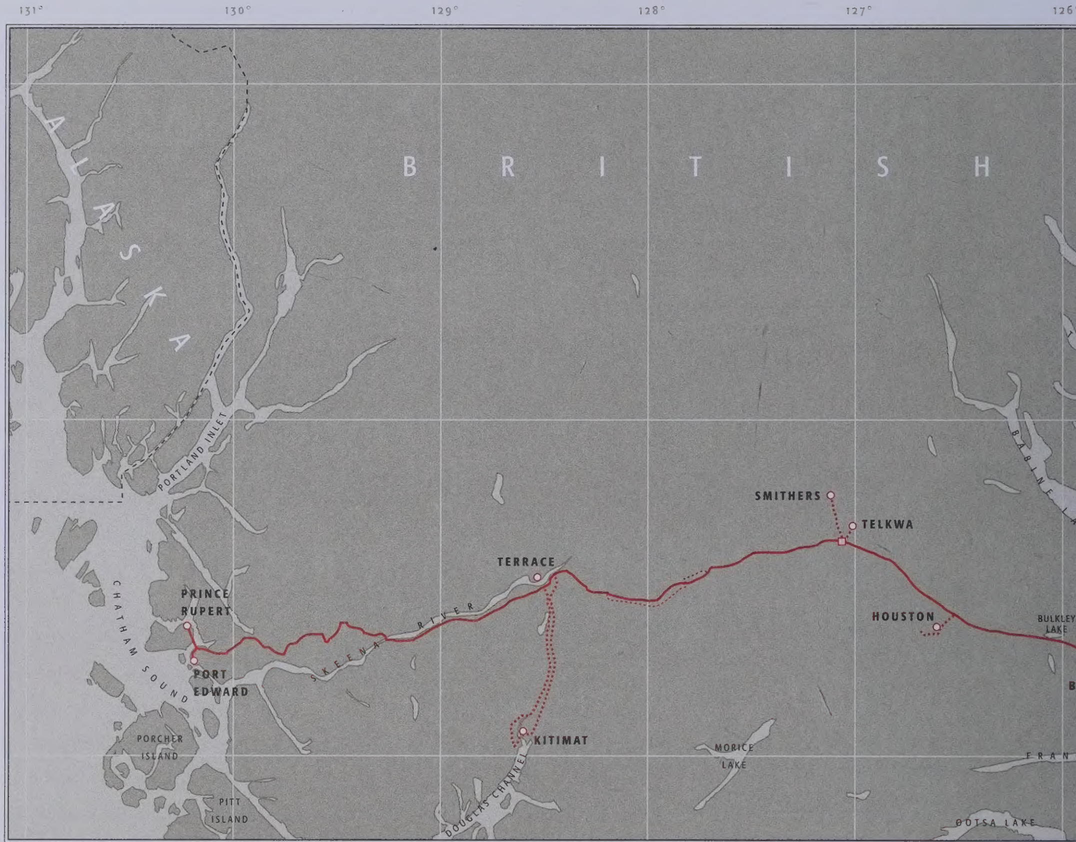
Port Edward / Ridley Island

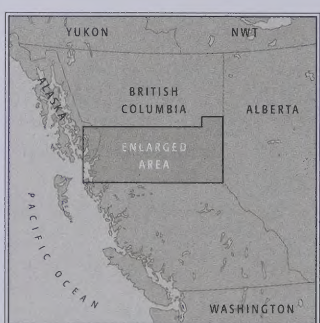


Kitimat

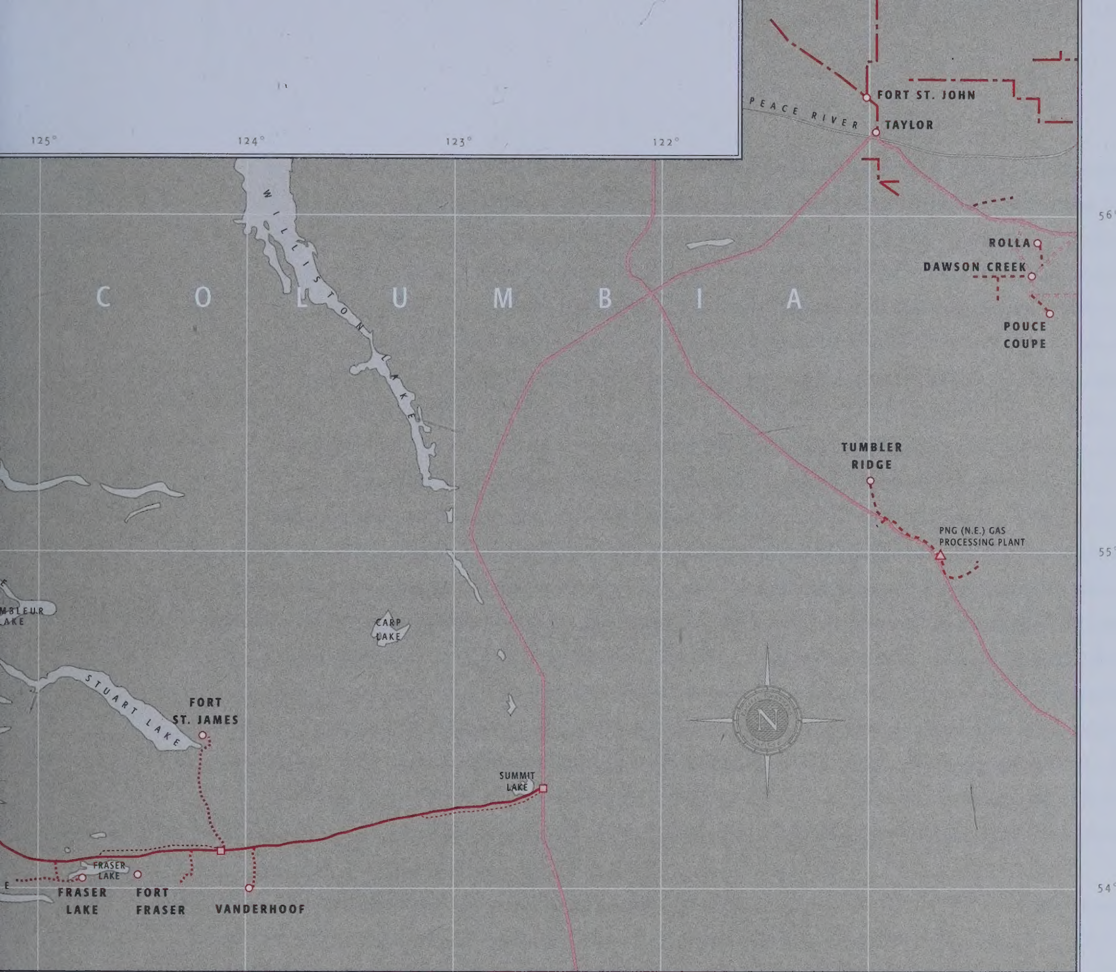


Houston





Pacific Northern Gas Mainline
Pacific Northern Gas Lateral Line
Mainline Looping
PNG (N.E.)
Centra Gas Fort St. John
Westcoast Energy Inc.
Peace River Transmission Company
Compressor Station



The Company

Pacific Northern Gas Ltd. delivers natural gas to customers in west-central British Columbia and through its subsidiaries, Pacific Northern Gas (N.E.) Ltd. and Centra Gas Fort St. John Inc., to customers in the province's northeast.

Pacific Northern's transmission pipeline is connected to the Westcoast Energy system near Summit Lake, British Columbia and extends 365 miles to the west coast. Service is provided to over 21,000 customers in 11 communities and to a number of large industrial operations.

Pacific Northern Gas (N.E.) systems serve 6,600 customers in the Dawson Creek and Tumbler Ridge areas. Gas supply for the Dawson Creek area is received from the Westcoast Energy system via the Peace River Transmission Company pipeline. In Tumbler Ridge the Company operates its own gas processing facility.

In early 1997 Pacific Northern acquired the 8,000 customer Centra Gas Fort St. John system. Gas supply is received from several points on the Westcoast Energy system.

Pacific Northern and its subsidiaries maintain service offices in 11 communities. Most of these locations also provide an operating base for construction crews and the personnel responsible for the operation and maintenance of the Company's compressor stations and gas plant. Marketing and administrative functions are supported from regional centres in Terrace, Dawson Creek and Fort St. John. The Company's head office is located in Vancouver, British Columbia.

PACIFIC NORTHERN GAS LTD. achieved record earnings and gas delivery levels during 1996. Net income of $7.39 million surpassed the previous record of $6.60 million in 1994 by 11.9 percent.

After providing for preferred share dividends, earnings per common share during 1996 were $2.01. This compares with $1.67 and $1.80 in the past two years. The 1996 results are attributable to colder than normal weather in our service areas and high delivery levels to our large industrial customers.

In addition to strong financial performance, I am pleased to report a major expansion of the Company resulting from agreements on two acquisitions, as well as a record level of new customer connections.

Acquisitions

DURING 1996, Pacific Northern acquired Centra Gas Victoria Inc. and reached an agreement to acquire Centra Gas Fort St. John Inc.

The purchase of the outstanding shares of Centra Gas Victoria Inc. will enable Pacific Northern to utilize certain non-capital tax losses. The tax savings are estimated to have a current value to the Company of $1.6 million. It is anticipated these benefits will be realized over a three year period commencing in 1997.

The purchase of all the shares of Centra Gas Fort St. John Inc., owner of the natural gas distribution system in Fort St. John, was completed in January 1997. This acquisition added almost eight thousand accounts, expanding the Company's customer base by more than 25 percent, and substantially increasing our non-industrial deliveries. Cost savings for customers are expected as a result of the geographic proximity of the system to the Company's northeast service area.

The Fort St. John acqusition will add $15.1 million or 10 percent to the Company's rate base. The purchase is being funded with cash generated from operations and with short-term debt. In the case of Centra Gas Victoria, the Company issued junior preferred shares which will be redeemed as the tax savings are realized.

Market Expansion

CONTRIBUTING to the Company's growth in 1996 were high levels of main extension and service connection activity. A total of 86 miles of new distribution main was installed during 1996. Eleven of our main extensions received funding from the Canada/British Columbia Infrastructure Works Program. Residents in proximity to the new mains responded very positively to the availability of gas service to their areas. At the end of the year the Company was providing service to some 28 thousand customers, an increase of over 1,300 during the year.

Natural Gas Markets

NOTWITHSTANDING our expanding customer base, our industrial customers continue to be important to our success. The Company's four largest customers accounted for 80 percent of total deliveries in 1996. Through the year, they operated at or near capacity levels, as did a second tier of large forestry and mining customers. Among Pacific Northern's 20 largest industrial customers, 12 recorded the highest gas consumption of the past five years. The Company's strong financial performance during the past year is, to a large degree, a result of the success of these industrial customers.

Colder than average weather through much of the year resulted in high levels of gas sales to the Company's core market of residential and commercial customers. Heating degree days for the year were more than 10 percent higher than normal, and resulted in record core market delivery levels to every community served by the Company.

Regulatory Issues

THE Company submitted a rate application to the British Columbia Utilities Commission in late 1995. After settlement of the two previous applications through an alternative dispute resolution process, there was general agreement that the 1996 application should be the subject of a formal hearing. A public hearing was conducted in the spring of 1996. For

most rate classes there were only minor adjustments of tariffs as a result of the net impact of approved increases in revenue requirements, allowed rate of return on common equity, rate reallocation between customer classes, and declines in gas supply cost.

As in recent years, the allowed return on common equity was established in advance through a predetermined relationship to long-term government debt. Pacific Northern's allowed return was 11.75 percent in 1996, and has been adjusted to 11.0 percent for 1997.

During the year the Company filed a proposal with the Commission concerning revisions to its main extension policy and service connection charges. The proposal was accepted by the Commission in December and will be implemented in 1997. The revised policy will enhance our ability to extend gas service in the rural areas in which we operate. It will also enable the company to assist customers by providing loans to finance construction costs or the purchase of energy equipment.

At the request of the Commission, the Company withdrew its March application to offer customer services in the non-regulated business arena. Subsequently, the Commission indicated its desire to conduct a comprehensive assessment of the appropriate manner of involvement of regulated utilities or their non-regulated affiliates in non-traditional markets such as equipment supply and maintenance and insurance plans. This assessment was launched in October with a Commission-organized workshop on "retail markets downstream of the utility meter". It is being followed at this time by a written review process. The Commission has stated its intention to report its views on the issue during the first quarter of 1997.

All gas supplied to our core customers during the year was purchased at prevailing market prices. These purchases were backstopped by a Commission-approved risk management plan. The use of financial instruments helps to protect customers from price volatility.

The Company's application concerning 1997 rate changes in the PNG-West service area was the subject of an alternative dispute resolution process. The objective of this process was to reach an agreement satisfactory to interested parties without the need for a formal public hearing. All outstanding issues were successfully resolved and the agreement received Commission approval in February 1997.

Tariff adjustments for 1997 have been approved by the Commission for the Dawson Creek area and Tumbler Ridge. These relate to changes in the cost of gas and the allowed return on common equity. Tariff adjustments have also been approved for the Fort St. John distribution area.

Market Outlook

DESPITE recent increases in wellhead prices, natural gas continues to enjoy a significant price advantage relative to the competing energy sources available in our service area. Therefore, I foresee continuing growth of our core market deliveries in the years ahead. This growth will result from additional extensions of our distribution mains, as well as property development in areas already served with natural gas. The new main extension test and improvements to our financing program can also be counted upon to stimulate customer additions.

Industrial markets offer considerable potential for increased deliveries of natural gas. During the past year, several organizations requested information on availability and cost of large volumes of gas for delivery to projects being proposed in our service corridor. These, or similar projects, would require major expansions of our system through looping – the extension of pipe parallel to the original transmission line. Additional growth in small to medium industrial and large commercial markets will continue in response to maturation and diversification of the economic bases of the communities we serve.

Pacific Northern is well positioned to accommodate expansion. At the present stage of system develop-

ment, capacity gained through transmission line looping is relatively inexpensive to install and operate. Thus, the marginal cost of the additional capacity is significantly less than the average cost of existing capacity. In addition to providing attractive pricing for new customers, expansions of capacity and throughput can benefit our other customers as well.

Vision

PACIFIC NORTHERN's vision statement is reproduced on the inner front cover of this year's annual report. It sets the direction for the Company in an ongoing transformation of the organization to meet future challenges and opportunities. The vision statement takes into account our expectation of an increasingly competitive business environment. We look forward to this with enthusiasm.

Our track record of efficient, safe and reliable service over the past 28 years has created an excellent relationship with our customers. The talents of our personnel will be a valuable resource as we move to expand the range of service options we offer.

Recognizing the importance of our personnel to the Company's future, we are expanding opportunities for them to contribute toward and benefit from the Company's success. Programs are underway or planned for implementation within the next few months to enhance technical skills, customer service and environmental awareness; to strengthen internal communications; and to permit success sharing. Our objective is to assure that our people have the training, support and incentive to excel. We are confident the outcome will benefit our employees, customers and shareholders.

Recognition

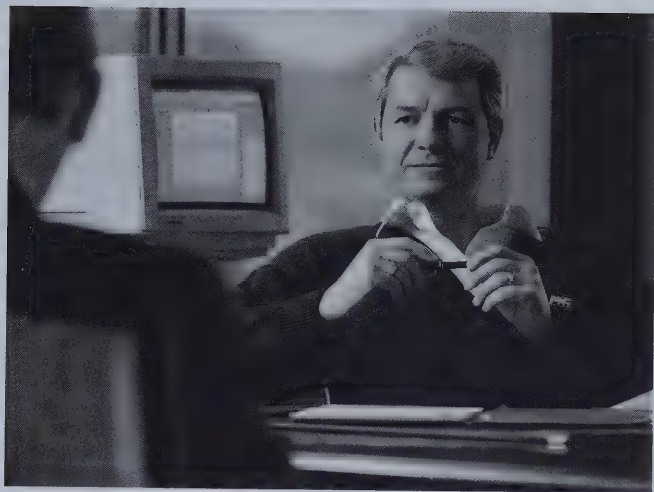
THE acquisition of operations that expand and complement our utility business was a highlight in 1996. I would like to recognize the work of the Special Committee of the Board of Directors in the review and negotiations that led to successful completion of these agreements. This committee of independent directors was chaired by Robert F. Chase, and included George Malpass, Hugh Morris and Robert O'Shaughnessy.

Also to be recognized are our employees. Their dedication on a daily basis is critical in maintaining high levels of service for our customers and performance for our shareholders. Their support makes my job an enjoyable one, and their talents and enthusiasm may be counted upon to support the Company's development in coming years.

On behalf of the Board of Directors

ROY G. DYCE
President and Chief Executive Officer

Vancouver, British Columbia
March 3, 1997



Roy G. Dyce

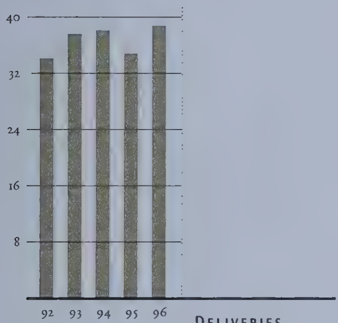
President and Chief Executive Officer

Fort St. James

Until recently sawmill trim cuttings were incinerated, under-utilizing forest resources and resulting in concern over air emissions. Since opening of Tl'Oh Forest Products in 1995, Fort St. James sawmills have been able to redirect a substantial volume of cuttings for finger-jointing into lumber for frame construction and millwork.

Recreational opportunities abound in the Fort St. James area: boating on Stuart Lake, river and lake fishing, hunting, back-road sightseeing, snowmobiling, down-hill and cross country skiing and golf. Among features enjoyed by a growing international clientele is the National Historic Park, located on the shore of Stuart Lake in Fort St. James.

Since extension of this main to the Nak'azdli Reserve in 1991 approximately 100 residents have obtained service connections. Overall in Fort St. James customer accounts have more than doubled since 1990, passing the 1,000 mark in early 1997.



Deliveries
Millions of Gigajoules

Record deliveries during 1996 were attributable to colder than normal weather during much of the year, and operations by our industrial customers which were mostly at or near capacity levels.

Financial Performance

During 1996 Pacific Northern earned a net income of $7.39 million, an increase of 19.3 percent over our 1995 earnings of $6.19 million. After providing for preferred share dividends, earnings per common share were $2.01, compared with $1.67 in the previous year.

Dividends paid to common shareholders were 96 cents per share compared with 94 cents in 1995. This increase reflects the full-year effect of the change in the quarterly dividend rate which was approved during 1995.

Operating Activities

Additions to property, plant and equipment totalled $9.8 million in 1996 compared with $14.3 million in 1995. In 1996 the Company's capital programs were directed almost entirely towards its retail distribution network, in contrast with 1995, which saw major improvements to its main transmission pipeline. During 1996, in addition to expenditures for normal customer growth, $2.8 million was expended to install distribution mains under the Canada/British Columbia Infrastructure Works Program.

Operating, maintenance and administrative costs totalled $13.4 million, an increase of $0.7 million over 1995. In addition to the higher costs associated with inflation and customer load growth, the Company experienced higher costs for gas used in operations than was the case in the previous year.

Acquisitions of two utility distribution systems and a transmission pipeline have been concluded and will add $15.5 million to the Company's rate base.

Gas Deliveries

Natural gas deliveries totalled 38.7 petajoules during 1996, compared with 34.7 petajoules in 1995. This record level was attributable to colder than normal weather in our service area during much of the year, as well as the operations of our large industrial customers which were mostly at or near capacity levels.

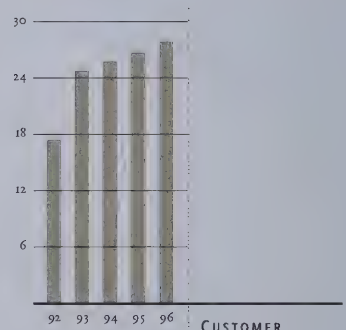
Our largest customer, Methanex Corporation, completed a scheduled three week maintenance shutdown at its Kitimat methanol/ammonia complex during the month of October. Subsequently, the customer encountered difficulties returning the plant to full production levels. Gas deliveries were about 20 percent below expectations in November, but had returned to normal levels by the month's end. Deliveries to Methanex during the year increased to 22.9 petajoules from the 21.6 petajoules delivered in 1995.

Throughout the year, both our pulp mill customers, Eurocan Pulp & Paper Co. and Repap British Columbia Inc., had gas requirements that met or exceeded expectations. Deliveries to the two customers totalled

7.3 petajoules, up from 5.6 petajoules in the previous year. Most other industrial transportation customers on the PNG-West system maintained or exceeded 1995 consumption levels. Total industrial deliveries for the year of 33.1 petajoules reflect an increase of over 11 percent from 1995.

Colder than normal weather resulted in record gas sales to core market residential and commercial customers on both the PNG-West and PNG(N.E.) systems. When adjusted to reflect average temperature conditions, sales rose modestly relative to the previous year.

Again in 1996 the Company was able to arrange the sale of gas to off-system customers when contracted gas supply was not required by core market customers. A total of 0.8 petajoules was sold off-system, down from a level of 2.1 petajoules in 1995. Revenue of $382 thousand from these sales will be credited to our core market customers through an adjustment in the 1997 rates.



Customer Accounts
YEAR END TOTALS IN THOUSANDS

A RECORD LEVEL OF OVER 1,300 NEW CUSTOMER ACCOUNTS WERE RECORDED DURING 1996.

Alternative Gas Delivery Services

"Buy / sell" arrangements previously in place between our commercial customers and a gas marketer were not renewed at the end of October 1996, and the Company reassumed responsibility for gas supply to these customers. Under the buy/sell arrangements the customer-appointed marketer had arranged gas supply, and the Company had paid the marketer its own weighted average cost of gas for the gas supplied by the marketer for delivery to the relevant customers.

Commencing in November 1996 a new rate schedule was added to the tariff to accommodate commercial sector customers on the PNG-West system who wish to arrange gas supply from a producer or marketer, and to contract with Pacific Northern for gas transportation service. The service is similar to that provided for the majority of our deliveries to industrial customers. To date seven customers have contracted for transportation service under the new tariff. The requirements of these larger customers represent approximately seven percent of total deliveries to the commercial sector.

Main Extension and Customer Additions

During 1996 the Company added 86 miles of distribution main to its system including 11 new mains which were supported with funding from the Canada/British Columbia Infrastructure Works Program. A record 1,340 new customers were added to the system during the year, up from 924 in 1995. Relatively high levels of new customer additions are anticipated during 1997 as additional residents with access to the infrastructure extensions apply for service connections.

VANDERHOOF

SAWLOGS ARE STOCKPILED FOR MILLING AT THE PLATEAU FOREST PRODUCTS MILL NEAR VANDERHOOF. THE FACILITY IS AMONG THE LARGEST OF 15 WOOD PRODUCT OPERATIONS SERVED BY PACIFIC NORTHERN. MOST USE SUBSTANTIAL VOLUMES OF NATURAL GAS IN DRY KILNS IN WHICH SAWN LUMBER IS DRIED TO MEET INDUSTRY SPECIFICATIONS.

USE OF FUSION TOOLS SPEEDS END-TO-END AND BRANCH JOINTS OF POLYETHYLENE DISTRIBUTION PIPE. COMPLETION OF THESE ROBUST JOINTS IS A ROUTINE ACTIVITY FOR PACIFIC NORTHERN CREWS AS THEY EXTEND THE 60 PSI DISTRIBUTION SYSTEM USING PIPES WITH DIAMETERS TO FOUR INCHES.

POLYETHYLENE DISTRIBUTION PIPE AND A TRACER WIRE ARE INSTALLED USING A VIBRATING PLOW. THE CONTRACTOR-OPERATED MACHINES ARE USED FOR LONGER MAIN EXTENSIONS. MUCH FASTER PIPE LAYING IS POSSIBLE THAN WITH THE TRADITIONAL OPEN TRENCH APPROACH – UP TO 1.5 MILES PER SHIFT WITH OPTIMAL GROUND CONDITIONS.

Smithers / Telkwa

The 4,500 HP Solar turbine compressor at Station R-4 near Telkwa provides sufficient pressure to move gas to the ends of distribution lines in Prince Rupert and Kitimat. Local personnel conduct checks and maintenance at each of the Company's four compressor sites, while control is provided from a remotely located gas control centre.

Four main extensions were installed in the Smithers area during 1996 under the Canada-British Columbia Infrastructure Works Program. Over 200 new customers were connected to these mains. The high level of activity is expected to continue through 1997.

Yard equipment at Pacific Inland Resources is used to move logs to the stockpile and the mill. Two large sawmills and a panel board plant are major contributors to the economy in the Smithers area.

Gas Supply and Pricing PACIFIC NORTHERN purchases all of its natural gas requirements in British Columbia. A long-term contract with CanWest Gas Supply Inc. accounted for over 80 percent of 1996 purchases. Most of the balance of the Company's requirements was purchased under firm gas contracts with two other suppliers. Small volumes were also purchased under seasonal and spot gas arrangements.

During 1996, the Company consolidated gas supply arrangements for the PNG-West and PNG(N.E.) systems. The Company also entered into an arrangement to use underground gas storage facilities in British Columbia on behalf of customers in the Dawson Creek area. The use of storage provides a hedge against volatile prices and an opportunity to minimize the cost of firm gas supply.

The pricing of the Company's portfolio of long-term gas supply is market based. Prices are determined monthly on the basis of price indices for British Columbia natural gas. Reflecting trends in continental markets and supply conditions in the Pacific Northwest, natural gas prices continued at low levels for the first three quarters of 1996. However, during November and December, the price of British Columbia gas more than doubled from levels during the same period in 1995. The situation reflects short-term market conditions. While prices may remain somewhat volatile, they are generally expected to decrease from these high levels in the near future.

A British Columbia Utilities Commission-approved risk management plan is operated to manage price volatility of a portion of the Company's gas supply portfolio. The Company continues to monitor market conditions and will enter into hedging arrangements as appropriate.

Regulatory Activities PACIFIC NORTHERN's regulator, the British Columbia Utilities Commission, conducted a public hearing in April to review the Company's revenue requirements in each of its service areas. Permanent rates were approved for the year, reflecting the revenue requirements decision as well as a number of adjustments relating to amortization of deferral accounts, rate design and flow through of natural gas costs.

In the PNG-West service area the 1996 rates for core market commercial and industrial customers and small industrial transportation customers declined substantially as a result of lower gas costs and rate design. Rates for residential customers and three of our four large industrial transportation customers were subject to modest increases.

On the PNG(N.E.) system, Dawson Creek residential customers experienced a small rate increase in 1996, while all other core market customers experienced rate reductions.

The Commission accepted the request of one of the Company's industrial customers to undertake a reconsideration hearing relating to the 1995 rate design decision. At issue was the treatment of gas contracted by the Company for core market customers which on a seasonal basis is surplus to their requirements. The gas is then available for sale on an interruptible basis to a number of industrial transportation customers. Reallocations resulting from the Commission's reconsideration resulted in a reduction of the revenue requirement attributed to industrial customers and a corresponding increase for residential customers, but did not affect the overall revenue requirement.

As a result of the Company's 1995 rate design decision the Commission agreed with the proposal that commercial customers should be permitted to select transportation service. A new rate schedule was added to the tariff effective November 1996 to provide these gas users with the option of purchasing their gas directly from producers or marketers and transporting it through the Company's system to their facilities.

In October the Commission sponsored a workshop on retail markets downstream of the utility meter. The objective was to permit interested parties to state their views on the involvement of utility companies or their affiliates in providing additional energy-related products and services in a non-regulated marketplace. Following the workshop the Commission issued a position paper and announced it would conduct a written review process. Interested parties were requested to file submissions and responses in early 1997. A decision has been scheduled for release in March 1997. Pacific Northern participated in the workshop and written review, and has indicated its desire for access to non-regulated markets.

The Commission's 1995 generic hearing into main extension policies was followed in 1996 by the issue of guidelines for main extension tests and policies relating to extensions and service connections. Pacific Northern filed proposed revisions to its test and policies. The proposal was accepted by the Commission in December. Modifications to the Company's tariff to reflect the changes are underway at present. Implementation of the new test and policy is planned in 1997. The new policy will increase the limit of the Company's investment in main extensions. It is expected to have a positive impact on the extension of gas service in the rural areas in which we operate. It will also make provision for Company financing of customer-borne costs of main extensions and service connections, providing new customers with the option of repayment in conjunction with their gas accounts.

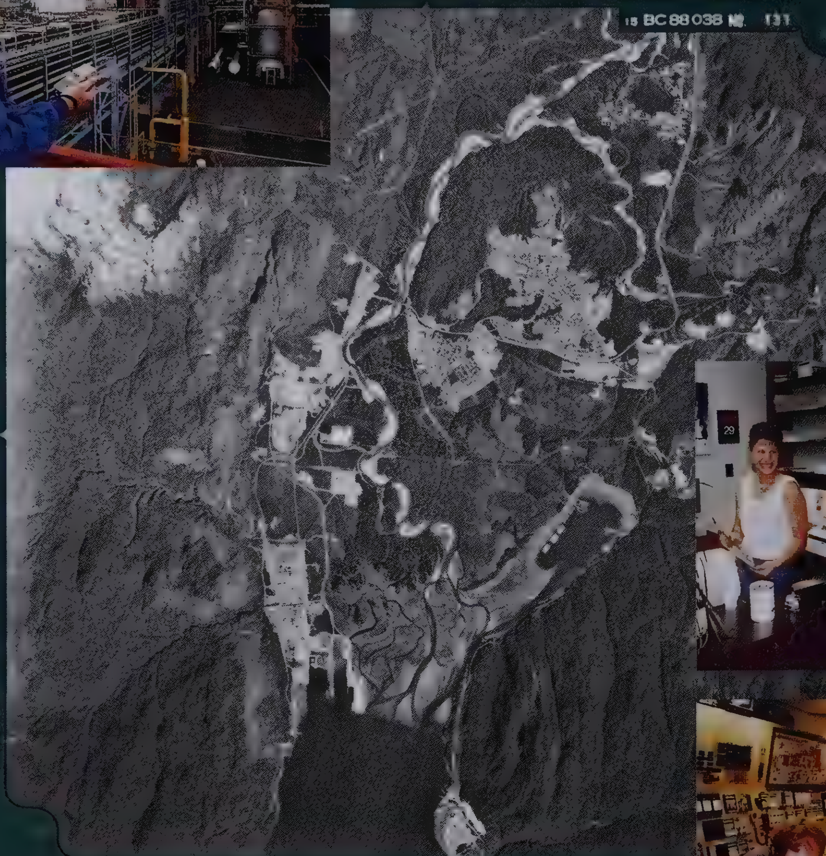
A 1997 revenue requirements application for the PNG-West system was filed with the Commission during November. Interested parties participated in an alternative dispute resolution process in January. All outstanding issues were successfully resolved. The resulting agreement received Commission approval in February, and will be reflected in adjustments to 1997 rates.

Terrace

The recently-opened Northern Healthcare building provides modern facilities for the community's medical and dental practitioners. It is the city's first five storey commercial building. Gas-fired hydronic heating and makeup air units were selected to assure a high level of comfort for building occupants.

In addition to a customer service centre, Pacific Northern's facilities in Terrace include a warehouse, pipe storage yard and fabrication shops. Most materials and equipment used on the western portion of the system moves through Terrace.

Fabrication activities include preparation of meter and regulator station sets and valve assemblies as well as custom built units for use in the Company's facilities and to support construction and maintenance operations.



Kitimat

Methanex Corporation's Kitimat methanol/ammonia plant is Pacific Northern's largest customer. Methanol production levels from this processing unit frequently exceed 1300 tonnes per day. Byproduct hydrogen from methanol production is utilized at the facility to support the production of anhydrous ammonia.

Permitting frequent personal contact with local residents, Pacific Northern's Kitimat service office is one of 11 maintained by the Company. These locations also provide an operating base for service and maintenance employees, and permit short-term storage of meters and supplies required for installation of service connections for new customers.

In the steam and recovery boiler control room at Eurocan Pulp & Paper Co. personnel oversee operation of the company's natural gas and hog fuel fired power boiler. The mill's daily output of kraft pulp typically exceeds 1200 tonnes, supporting prouction of premium quality unbleached kraft paper and linerboard.

Rate change applications for Dawson Creek and Tumbler Ridge were filed in December to reflect changes in the return on common equity and gas supply costs. These issues did not require a public review and the rate changes were approved effective January 1, 1997, along with interim rates for the PNG-West system.

Engineering and Operations

REHABILITATION of a 12 mile section of the eight inch transmission line between Terrace and Prince Rupert was completed during 1996. The work was coordinated with federal and provincial environmental agencies to assure protection of important salmon spawning habitat. With the appropriate machinery mobilized to the area, work also included development of an access trail to a remote section of the pipeline in preparation for work that is planned for 1998. The latter will include improved protection of the pipe and replacement of pipe sections identified in an electronic line survey.

During 1996 the Company replaced its supervisory control and data acquisition (SCADA) system. The new system provides real time data on operating conditions at each of the four compressor stations and a number of other key control and delivery points. It is interfaced with the system control centre, which is operated for Pacific Northern on a shared-service basis by Westcoast Energy, and also permits key personnel to monitor system operations on their computer terminals.

Operation of the new SCADA system will be complemented by replacement of control panels at each of the compressor stations. The first phase of this replacement program involved panel design, fabrication and installation at station R-3, Burns Lake during 1996. Plans call for completion of the project in 1997 with replacement of control panels at our other three compressor stations.

Stress Corrosion Cracking

STRESS corrosion cracking (SCC) is a phenomenon in which "colonies" of small cracks develop on the outside surface of a buried pipe. Over a period of years the cracks may lengthen, deepen and join together, ultimately reaching a point at which detection and remedial action is required to assure integrity of the pipeline.

SCC was confirmed as the cause of the 1995 failure of the Company's mainline at a location 2.5 miles downstream from compressor station R-1, located near Summit Lake. Failures on high pressure pipelines of other gas transmission companies have also been attributed to SCC, and the phenomenon has been the subject of a recent review by the National Energy Board. While causes are not fully understood,

the soil and pipe coating conditions that promote SCC are being identified. These provide the industry with useful guidance on where to focus SCC investigations.

As a result of its own experience as well as the industry's general concern, Pacific Northern initiated a stress corrosion cracking management program in 1996. Several activities were completed during the year. First, a consultant reviewed and interpreted terrain and soil conditions to identify the zones traversed by the mainline that would be most prone to SCC. This information was correlated with data from a previous electronic inspection of the mainline as a basis for identification of pipe sections for digout inspections. During the 14 digouts, several zones of affected pipe were either replaced or restored through a buffing and recoating process.

Hydrostatic testing of the 12 mile section of the original mainline downstream of compressor station R-1 followed completion of the digouts. Five additional pipe sections were replaced prior to achieving a test pressure of 138 percent of the maximum operating pressure, a level well above the required minimum for hydrostatic testing of natural gas transmission lines.

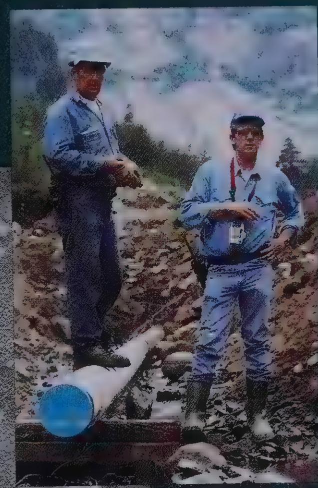
Plans have been made for continuation of the Company's SCC program during 1997. Twelve miles of pipeline loop downstream from Summit Lake will be the subject of an internal electronic inspection. Also, digout inspections of pipe will be conducted downstream from each of the other compressor stations.

SCC will remain an issue for the Company in the years ahead. Fortunately, susceptibility appears to be limited to small portions of the transmission system. Based on experience gained during 1996 and hydrostatic test results, management is confident that the Company has implemented an appropriate program to assure the long-term integrity of the system.

Environment and Safety

PROGRAMS are continuing to assure all employees are fully trained and aware of the Company's commitment to environmental responsibility. During the year our personnel worked with others in the Westcoast Group of Companies to develop a comprehensive, eight module training program. The product has received recognition from the Canadian Energy Pipeline Association. Over a two year period commencing in February 1997 all employees will be involved in training sessions which will include program modules relevant to their duties.

Gas compressor station sites were the focus of a 1996 joint Pacific Northern and Westcoast Energy environmental audit. The Company's current operating practices were generally endorsed. As appropriate, steps have been taken to implement improvements.



Khyex / Skeena River Confluence

During 1996, the Company replaced several sections of the transmission line leading along Arden Creek towards the Khyex River. Erosion had exposed portions of the original pipe, increasing the risk of disruption by landslides and avalanches.

In some cases reinforcement of the existing pipe is preferable to pipe replacement. At a point five miles upstream of the Khyex/Skeena confluence a fiberglass sleeve is added to overcome the effect of mild surface corrosion. There is no venting of gas to the atmosphere and the line remains in service throughout the procedure.

A contractor uses a theodelite to survey the right of way in proximity to the route of a section of replaced pipe. Local sourcing is encouraged for requirements of this type, supporting community business enterprises, and providing expedient and cost effective service.

Prince Rupert

Cars of a unit train loaded with coal from Tumbler Ridge enter the thaw shed at Ridley Island Terminals. In winter months natural gas-fired heaters are used to thaw coal which has frozen into the rail cars. After passing through the shed the rail cars are dumped and the coal is either stockpiled or transferred to a waiting ship.

Salmon is prepared for market at J.S. McMillan Fisheries in Prince Rupert. The facility is one of the largest fish processors on the British Columbia coast with seasonal handling of salmon, halibut, herring and crab. Fresh, frozen and canned products are shipped from the plant to international markets.

New homes in Prince Rupert's popular new Eagle Heights Subdivision. In recent years there has been strong housing construction activity in Pacific Northern's service area. Subdivisions fill quickly. Natural gas is the fuel of choice in new homes for space and water heat and open-flame fireplaces.

A progress report was filed and the Company is continuing its participation in Canada's Climate Change Voluntary Challenge Program. With increasing gas deliveries, in part as a result of substitution of natural gas for fuels with higher carbon dioxide and pollutant levels, higher volumes of fuel consumption will occur at the Company's compressor stations. However, in other aspects of the Company's operations, steps are being taken to reduce greenhouse gas emissions. These include the use of a fiberglass sleeve pipe reinforcement technique as an alternative to the removal and replacement of sections of the transmission pipeline and the installation of bypass valves and pipe to minimize blowdown releases during maintenance operations. Also a policy is being implemented to flare gas in order to avoid atmospheric release of methane during the course of work on distribution lines.

The Company continues to stress the importance of safe operating practices. No lost time accidents were experienced in 1996, and the Company continues to maintain a leading position among Canadian gas utilities with respect to both lost time and motor vehicle accidents.

Liquidity and Capital Resources

THE Company's investment activities are financed by cash generated from operations, together with proceeds from the issue of long-term debt and share capital. Funding is also provided by customers and government agencies where estimated revenues are insufficient to support the required capital expenditures. During 1996, government contributions of $1.35 million were received under the Canada/British Columbia Infrastructure Works Program towards the cost of installing distribution mains.

During 1996, the Company issued cumulative redeemable junior preferred shares in the amount of $13.91 million in exchange for losses of an associated company which are expected to generate income tax savings of $15.46 million. As these tax savings are realized, the junior preferred shares will be redeemed by Pacific Northern.

Pacific Northern has a bank line of credit in the amount of $35 million which provides working capital as well as interim financing for its capital programs.

Through its parent company, Westcoast Energy Inc., Pacific Northern has access to commercial paper money markets. The Company obtains its short-term borrowing requirements from this source when it is financially advantageous to do so.

Alternative Dispute Resolution
A process in which interested parties seek an agreed settlement of issues without the need for a formal public hearing.

British Columbia Utilities Commission
This provincially appointed body regulates capital programs, operations and earnings of the energy utilities in British Columbia.

Buy/sell
An arrangement where an independent gas marketer acquires gas on behalf of core market customers and arranges for its delivery to the Company's system.

Core market
Residential, commercial and small industrial customers for whom the Company plans and arranges gas supply and transmission and distribution capacity to meet peak requirements.

Firm Gas
The industry term for gas which must be delivered without interruption under contractual obligations. It is gas guaranteed to be delivered regardless of fluctuations in seasonal demand.

Gigajoule (GJ)
A metric measurement of energy used for routine customer billing; one billion joules.

Terajoule (TJ)
one thousand gigajoules

Petajoule (PJ)
one million gigajoules

Interruptible sales/service
Delivery of natural gas subject to the availability of gas supply and capacity on the Company's system. Sales involve gas surplus to the requirements of core market customers, or purchased by the Company in the spot market. Service involves delivery of gas supply arranged by the customers in excess of the volume for which they have contracted for firm delivery by the Company.

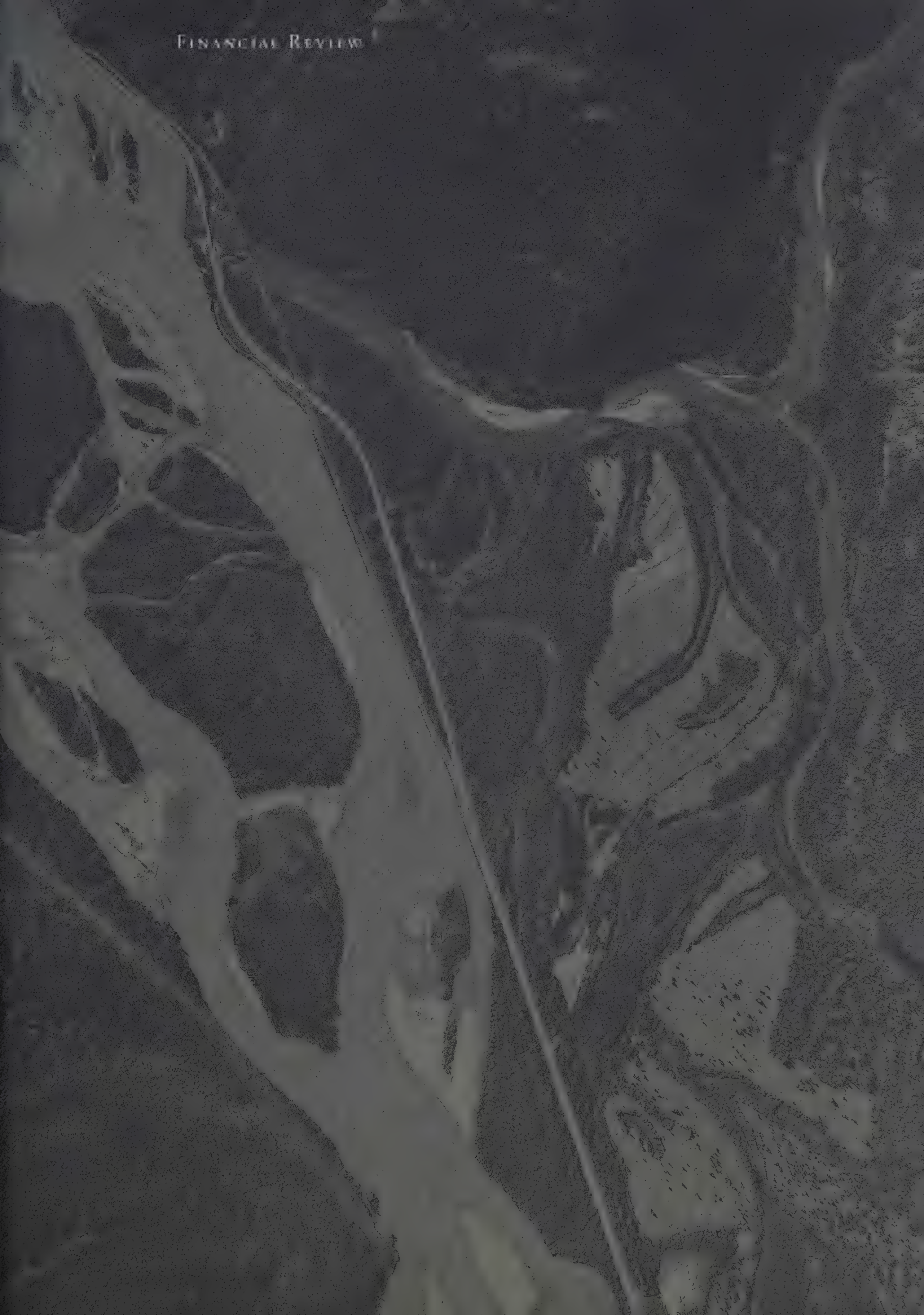
Looping
The addition of a second pipe connected in parallel to an existing pipeline to increase capacity through a reduction in pressure loss.

Off-system sales
Sale of natural gas contracted by the Company, and periodically surplus to the requirements of core market customers, to purchasers who will obtain delivery through other pipeline systems.

Transportation customers
Large industrial and commercial customers who contract with the Company for pipeline capacity and make their own arrangements for supply of gas and its delivery to the Company's system.

Metric to Imperial Conversions

1.0 GJ	=	0.94782 MMBtu
1.0 $10^3 m^3$	=	35.301 Mcf



he Shareholders of
ific Northern Gas Ltd.

WE have audited the consolidated balance sheets of Pacific Northern Gas Ltd. as at December 31, 1996 and 1995 and the consolidated statements of income, retained earnings and cash flow for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 1996 and 1995 and the results of its operations and the changes in its financial position for the years then ended in accordance with generally accepted accounting principles. As required by the Company Act of British Columbia, we report that, in our opinion, these principles have been applied on a consistent basis.

ERNST & YOUNG
Chartered Accountants

Vancouver, Canada
January 27, 1997

RESPONSIBILITY FOR FINANCIAL STATEMENTS

THE accompanying financial statements were prepared by management of the Company in conformity with generally accepted accounting principles applied on a consistent basis. Management is responsible for the integrity and objectivity of the information contained in the financial statements. Management is also responsible for installing and maintaining appropriate internal controls, policies and procedures, which provide reasonable assurance that reliable financial information is produced and that the Company's assets are safeguarded. Ernst & Young, Chartered Accountants, as the Company's external auditors appointed by the shareholders, have examined the financial statements for the years ended December 31, 1996 and 1995, in accordance with generally accepted auditing standards and rendered their independent opinion thereon. The Audit Committee of the Board of Directors meets with the external auditors to review the manner in which they are performing their responsibilities and to discuss auditing, internal accounting controls and financial reporting matters. The external auditors have full access to the Audit Committee of the Board.

Years ended December 31 *(thousands of dollars)*		1996		1995
Operating revenues [notes 1 and 9]	$	62,823	$	60,998
Cost of sales [note 9]		14,975		19,943
Operating margin		47,848		41,055
Operating and maintenance		9,335		8,728
Administrative and general		4,083		3,954
Amortization of deferred charges		1,512		1,128
Municipal and other taxes		3,193		3,836
Depreciation		5,280		4,518
		23,403		22,164
Operating income		24,445		18,891
Investment and other income		117		125
		24,562		19,016
Income deductions:				
Interest on long term debt		8,369		8,037
Other interest		570		1,003
		8,939		9,040
Income before income taxes		15,623		9,976
Income taxes [note 3] – currently payable		5,568		5,251
– deferred		2,670		(1,466)
		8,238		3,785
Net income for the year	$	7,385	$	6,191
For common shares				
Net income for the year	$	7,385	$	6,191
Provision for dividends on preferred shares		337		337
Net income applicable to common shares	$	7,048	$	5,854
Per common share [note 5]				
Basic	$	2.01	$	1.67
Fully diluted	$	1.98	$	1.65

See accompanying summary of accounting policies and notes

As at December 31 *(thousands of dollars)*	1996	1995
Assets [note 8]		
Current assets		
Accounts receivable [note 1]	$ 12,635	$ 10,306
Inventories of supplies and natural gas	1,191	193
Prepaid expenses	613	609
	14,439	11,108
Plant, property and equipment [note 2]	168,493	165,149
Deferred charges		
Debt expense	817	865
Pipeline rehabilitation costs	3,049	3,137
Other	1,902	1,058
	5,768	5,060
	$ 188,700	$ 181,317

On behalf of the Board:

Director

Director

As at December 31 *(thousands of dollars)*

	1996	1995
LIABILITIES		
Current liabilities		
Bank indebtedness	$ 259	$ 225
Note payable to Westcoast Energy Inc. [note 9]	11,800	7,200
Accounts payable and accrued liabilities	9,249	6,591
Income and other taxes payable	1,531	2,957
Long term debt due within one year [note 8]	5,187	3,937
	28,026	20,910
Long term debt [note 8]	74,862	80,056
Deferred income taxes [note 6]	1,863	15,514
Contributions in aid of construction	10,254	8,799
	115,005	125,279
Commitments [note 10]		
SHAREHOLDERS' EQUITY		
Preferred shares [note 6]	18,910	5,000
Common shares [note 7]	8,774	8,757
Contributed surplus [note 7]	1,712	1,662
Retained earnings	44,299	40,619
	54,785	51,038
	73,695	56,038
	$ 188,700	$ 181,317

See accompanying summary of accounting policies and notes

Consolidated Statements of Retained Earnings

Years ended December 31 *(thousands of dollars)*	1996	1995
Balance, beginning of year	$ 40,619	$ 38,057
Net income for the year	7,385	6,191
	48,004	44,248
Preferred dividends	337	337
Common dividends	3,368	3,292
	3,705	3,629
Balance, end of year	$ 44,299	$ 40,619

See accompanying summary of accounting policies and notes

Consolidated Statements of Cash Flow

Years ended December 31 *(thousands of dollars)*	1996	1995
Operating Activities		
Net income for the year	$ 7,385	$ 6,191
Add (deduct) items not involving cash:		
Deferred income taxes	2,670	(1,466)
Depreciation and amortization	6,792	5,646
Other	(4,378)	1,872
Operating cash flow	12,469	12,243
Non-cash working capital changes	(1,242)	1,896
Net cash provided by operating activities	11,227	14,139
Investing Actvities		
Additions to plant, property and equipment	(8,916)	(13,675)
Deferred charge expenditures	(1,032)	(1,933)
Acquisition of Centra Gas Victoria Inc. [note 6]	(13,910)	—
Net cash used by investing activities	(23,858)	(15,608)
Financing Activities		
Issue of long term debt	—	20,000
Repayment of long term debt	(3,944)	(3,934)
Issue of common shares	67	44
Issue of junior preferred shares [note 6]	13,910	—
Contributions in aid of construction	1,669	168
Dividends paid	(3,705)	(3,629)
Net cash provided by financing activities	7,997	12,649
Increase (decrease) in cash position during the year	(4,634)	11,180
Cash position, beginning of year	(7,425)	(18,605)
Cash position, end of year	$ (12,059)	$ (7,425)

Cash position comprises bank indebtedness and the note payable to Westcoast Energy Inc.
See accompanying summary of accounting policies and notes

Principles of Consolidation
The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Pacific Northern Gas (N.E.) Ltd. and PNG Marketing Ltd.

Regulation
The Company and Pacific Northern Gas (N.E.) Ltd. are regulated utilities engaged in the transportation and distribution of natural gas. Their accounting records and practices conform to the requirements of the British Columbia Utilities Commission ("the Commission").

Plant, Property and Equipment
Plant, property and equipment are recorded at cost. Cost includes an allowance for funds used during construction calculated at the Company's cost of capital. The cost of depreciable assets retired, together with removal costs, less salvage is charged to accumulated depreciation. Gains or losses on disposal are not taken into income unless the disposal is outside the normal course of business or involves a major item of plant.

Depreciation is provided on a straight-line basis for plant in service at the commencement of each fiscal year at rates prescribed by the Commission. Average annual depreciation rates are 2.6% [1995 - 2.3%] for transmission plant, 2.4% [1995 - 2.2%] for distribution plant, 5.8% [1995 - 7.2%] for general plant and 4.9% [1995 - 4.9%] for processing plant. Application of these rates for the year ended December 31, 1996 resulted in a composite rate of 2.7% [1995 - 2.5%].

Inventories of Supplies and Natural Gas
Inventories are valued at the lower of cost determined on a first-in, first-out basis and net realizable value.

Deferred Charges
[a] Debt expense
Debt expense comprises issue costs of long term debt which are amortized over the term of the related issue.

[b] Pipeline rehabilitation costs
Pipeline rehabilitation costs are being amortized on a straight-line basis over ten years. The amount of such amortization in 1996 was $529,000 [1995 - $488,000].

[c] Other
Other deferred charges include costs incurred in the conversion of customers' equipment for the use of natural gas and certain application and regulatory costs, which are amortized over periods of up to ten years. In respect of these costs, an amount of $983,000 was charged to income during 1996 [1995 - $640,000].

Contributions in Aid of Construction
Where estimated revenue is less than the cost of providing service, additions to utility plant are made with the assistance of contributions from customers and government agencies. These amounts are amortized at a composite rate of 2.9% [1995 - 2.7%] per annum by an offset against the provision for depreciation of the assets to which they relate.

Income Taxes
In accordance with Commission directives, the Company followed the tax allocation method of accounting for income taxes from July 1, 1978 through November 6, 1986. Under this method, reported earnings are charged with the income taxes related to those earnings. Differences between these taxes and taxes currently payable, resulting principally from differences in the timing of expense deductions, are recorded as Deferred Income Taxes.

Inclusion of the deferred income tax component in customer rates has been suspended by Order of the Commission, effective November 7, 1986.

The tax allocation method is followed by Pacific Northern Gas (N.E.) Ltd. and this method will continue to be followed by the Company in respect of certain specific transactions as directed by the Commission and its non-regulated activities.

Had the Company followed the tax allocation method prior to July 1, 1978 and subsequent to November 6, 1986, deferred income taxes recorded in the accounts would have been increased by approximately $15,422,000 [1995 - $15,449,000].

Pension and Other Post-Retirement Employee Benefits
Pension costs and obligations are determined annually by independent actuaries using management's best estimates. Pension expense consists of current service costs and adjustments arising from plan amendments, changes in assumptions, and experience gains or losses which are amortized on a straight-line basis over the expected average remaining service life of the plan members.

Certain health care and life insurance benefits are provided for employees after retirement. The cost of these benefits is expensed as incurred.

1. Major Customers

The proportion of energy deliveries and revenues attributable to large industrial customers is as follows:

Percent	1996		1995	
	Energy	Revenue	Energy	Revenue
Methanex Corporation	58	37	59	36
Repap British Columbia Inc., Eurocan Pulp and Paper Co. and Alcan Smelters and Chemicals Ltd.	21	17	17	14

At December 31, 1996, 40% [1995 - 29%] of accounts receivable was attributable to these four large industrial customers.

2. Plant, Property and Equipment

Thousands of dollars	1996	1995
Transmission plant	$ 148,621	$ 144,572
Distribution plant	61,135	55,776
General plant	11,492	11,054
Processing plant	2,525	2,525
Construction in progress	1,244	1,929
Total plant, property and equipment	225,017	215,856
Accumulated depreciation		
Transmission plant	37,576	33,644
Distribution plant	13,111	11,823
General plant	4,346	3,872
Processing plant	1,491	1,368
Total accumulated depreciation	56,524	50,707
	$ 168,493	$ 165,149

3. Income Taxes

Income tax expense varies from the amount that would be expected if current rates were applied to income before income taxes for the following reasons:

Percent	1996	1995
Corporate income tax rate	45.6	45.6
Large corporations tax	2.6	3.8
Depreciation in excess of capital cost allowance	0.2	(2.4)
Deferred taxes recorded in the accounts	17.3	(14.6)
Deferred charge expenditures	(11.6)	3.7
Other items	(0.9)	1.8
Income tax rate recorded in the accounts	53.2	37.9

4. Pension Plans

The Company and its subsidiaries have defined benefit pension plans covering substantially all employees. The plans provide benefits based on length of service and earnings. Pension costs of $651,000 were charged to operations during 1996 [1995 - $750,000]. At December 31, 1996, the actuarial estimate of the present value of accrued pension benefits was $9,134,000 [1995 - $9,450,000], and the market value for actuarial purposes of the assets available to provide these benefits was $8,844,000 [1995 - $8,225,000].

5. Earnings Per Common Share

Earnings per common share have been calculated after deducting preferred share dividend requirements from net income. Earnings per share on a fully diluted basis were calculated after allowing for the exercise of employees' options on Class A common shares.

Net income used in determining fully diluted earnings per common share has been increased by $40,000 in 1996 [1995 - $51,000] to give effect to an imputed after tax return of 3.1% [1995 - 3.7%] on funds which would have been available on the exercise of options.

6. Preferred Shares

Thousands of dollars		1996	1995
Authorized			
200,000	6¾% cumulative redeemable preferred shares with a par value of $25 each		
1,400,000	cumulative redeemable junior preferred shares with a par value of $10		
Issued			
200,000	6¾% preferred shares	$ 5,000	$ 5,000
1,390,983	junior preferred shares	13,910	—
		$ 18,910	$ 5,000

The 6¾% preferred shares are redeemable at the option of the Company at $26 per share plus any accrued and unpaid dividends at the date of redemption.

During December 1996, the Company issued 1,390,983 junior preferred shares in the amount of $13,909,821 as consideration for the acquisition of all of the outstanding shares of Centra Gas Victoria Inc., a company related through common control. Prior to December 31, 1996, Centra Gas Victoria Inc. was wound up and the net assets were distributed to the Company. The net assets consist of the benefits relating

to non-capital loss carryforwards deductible under the Income Tax Act. The junior preferred shares are recorded at the amount negotiated by an independent committee of the Board of Directors, equivalent to 90% of the tax savings expected to be realized upon the utilization of the non-capital loss carryforwards.

The junior preferred shares are redeemable on a quarterly basis commencing March 31, 1997 in amounts equal to 90% of the estimated tax savings realized during the preceding quarter from the utilization of non-capital loss carryforwards. The Company may, at its option, satisfy the redemption requirements of the junior preferred shares by issuing Class A non-voting common shares of the Company at an issue price per common share of 85% of the weighted average trading price of the Class A non-voting common shares for the 20 business days preceding the date of the notice of redemption.

7. *Common Shares*

Thousands of dollars		1996	1995
Authorized			
6,000,000	Class A non-voting common shares with a par value of $2.50 each		
20,000	Class B voting common shares with a par value of $2.50 each		
Issued			
3,489,760	Class A common shares [1995 - 3,482,860]	$ 8,724	$ 8,707
20,000	Class B common shares	50	50
		$ 8,774	$ 8,757

During 1996, the Company issued 6,900 [1995 - 4,300] Class A common shares for cash consideration of $67,000 [1995 - $44,000] upon the exercise of employee options. Of this amount, $50,000 [1995 - $34,000] representing the excess of the issue price over the par value of the shares has been credited to contributed surplus.

The following Class A common shares are reserved for issuance upon the exercise of options by employees:

Number of shares	*Option price*	*Option expires*
9,600	$ 9.6875	February 5, 1998
14,560	10.7500	April 27, 2000
6,880	14.1250	January 28, 2002
8,600	15.7500	May 4, 2003
38,100	20.0000	November 7, 2005
24,400	19.0000	March 14, 2006

8. *Long Term Debt*

Thousands of dollars	1996	1995
Secured Debentures		
1997 Series, 18% due May 1, 1997, payable in annual instalments of $1,925,000 with a final instalment of $2,475,000 at maturity.	$ 2,475	$ 4,400
2002 Series, 10.85% due July 15, 2002, payable in annual instalments of $2,000,000 commencing July 15, 1994, with a final instalment of $12,000,000 at maturity.	22,000	24,000
2011 Series, 10.75% due December 13, 2011, payable in annual instalments of $700,000 commencing June 13, 1997 and $800,000 in each of years 2009 and 2010 with a final instalment of $5,000,000 at maturity.	15,000	15,000
2018 Series, 8.75% due November 15, 2018, payable in annual instalments of $600,000, commencing November 15, 1999 and $1,000,000 in each of the years 2014 to 2017, with a final instalment of $7,000,000 at maturity.	20,000	20,000
2025 Series, 9.30% due July 18, 2025, payable in annual instalments of $500,000, commencing July 18, 2004 with a final instalment of $9,500,000 at maturity.	20,000	20,000
Construction advances	574	593
	80,049	83,993
Deduct long term debt due within one year shown as a current liability	5,187	3,937
	$ 74,862	$ 80,056

[a] Collateral for the Company's Secured Debentures consists of a specific first mortgage on substantially all of the Company's fixed assets, gas purchase and gas sales contracts, and by a first floating charge on other property, assets and undertakings.

8. Long Term Debt (cont'd.)

[b] Payments required to meet sinking fund and retirement provisions during the next five years are as follows:

Thousands of dollars	
1997	$ 5,175
1998	2,700
1999	3,300
2000	3,300
2001	3,300

[c] Advances have been received from certain industrial concerns to enable construction of the facilities required to provide natural gas service. This financing is non-interest bearing and will be repaid as these customers meet their commitments for the purchase of natural gas.

9. Related Party Transactions

(see also notes 6 and 12)

The Company's transactions with related parties are as follows:

Thousands of dollars	1996	1995
Westcoast Energy Inc., parent company		
Transportation services	$ 506	$ 391
Materials and services	494	458
Interest on note payable	332	861
Westcoast Gas Services Inc., a company related through common control		
Natural gas purchases and services	410	308
Sales	967	1,931

These transactions are in the normal course of operations and are recorded at amounts established and agreed between the related parties.

The note payable to Westcoast Energy Inc. is due on demand and bears interest at the cost of funds of Westcoast Energy Inc. plus 0.0625% which at December 31, 1996 was 3.39% [1995 - 6.13%].

10. Natural Gas Swap Contracts

The Company's tolls are set using a forecasted price for gas. However, the Company's gas supply contracts contain pricing mechanisms that reflect monthly variations in the price of gas, rather than fixed prices. At December 31, 1996, the Company has entered into natural gas price swap contracts to effectively fix the price for approximately 20% of its forecast 1997 system gas supply. The difference between the price of gas used for toll purposes and the actual cost of gas purchased is deferred and refunded to or recovered from customers as directed by the Commission. The swap contracts have a fair value of $1,895,000 receivable at December 31, 1996 [$93,000 payable at December 31, 1995]. The fair value reflects the estimated amount that the Company would receive to terminate the swap contracts at December 31, 1996, based on the estimated future net cash flows under the terms of each contract.

11. Fair Values of Financial Instruments

The fair values of debt instruments included in the consolidated balance sheets are as follows:

	Carrying value		Fair value	
Thousands of dollars	1996	1995	1996	1995
Bank indebtedness	$ 259	$ 225	$ 259	$ 225
Note payable to Westcoast Energy Inc.	11,800	7,200	11,800	7,200
Long term debt	80,049	83,993	93,265	93,663

The fair values of the bank indebtedness and the note payable to Westcoast Energy Inc. approximate their carrying values.

The fair values of the Company's long term debt are estimated by reference to quoted market prices for actual or similar instruments.

12. Subsequent Events

[a] The Company has applied for changes to its rates effective January 1, 1997. The allowed return on common equity for 1997 has been set at 11.00% [1996 - 11.75%].

[b] Effective January 1, 1997, the Company acquired all of the outstanding preferred and common shares of Centra Gas Fort St. John Inc., a company related through common control, and an $8,000,000 loan owing by Centra Gas Fort St. John Inc. to Centra Gas Inc., a company also related through common control. The purchase price consisted of cash of approximately $14,906,000, including costs of acquisition. The acquisition was measured at the exchange amount, which was negotiated by an independent committee of the Board of Directors. Concurrently, the Company became party to an interest rate swap contract that converts the interest rate characteristics of $8,000,000 of short-term borrowings from floating to a fixed rate of 7.70%.

The bylaws of the Toronto Stock Exchange ("TSE") require that the Corporation disclose the corporate governance practices of its Boards of Directors ("Board"). The following report addresses the principal responsibilities of a board of directors contained in the guidelines for corporate governance established by the TSE.

Through its Nominating and Corporate Governance Committee (the "Committee") the Board will develop sound corporate governance practices to enhance shareholder value.

Board of Directors

The Board, as set out in its terms of reference, has the responsibility for overseeing the conduct of the business of the Company and the activities of management which is responsible for the day to day operations of the business.

Composition of the Board

The Board is composed of nine directors. One of the directors is a full-time officer and three are full-time officers of the Company's parent, Westcoast Energy Inc. ("Westcoast"), which owns 100% of the voting common shares and is therefore considered a significant shareholder. The TSE Guidelines provide that a director related to a significant shareholder should not be considered a related director of the subsidiary company. The remaining five directors do not have interests in or relationships with the Company or its parent (other than interests and relationships arising from shareholdings) which could, or could reasonably be perceived to materially interfere with such directors' ability to act with a view to the best interests of the Company. The Board has concluded that a majority of the directors of the Company are outside and unrelated.

Committees of the Board

The Board has established and adopted terms of reference for each of the Audit, Executive, Environment, Compensation and Nominating and Corporate Governance Committees.

The Audit Committee is composed of unrelated directors, of whom a majority including the Chair are outside directors. One of the three committee members is a full-time officer of Westcoast. This committee is broadly responsible for ensuring that the Company's management has designed and implemented an effective system of internal financial controls, for reviewing and reporting on the integrity of the consolidated financial statements of the Company, for ensuring compliance with regulatory and statutory requirements as they relate to financial statements, taxation matters and the disclosure of material facts and for reviewing the appropriateness and effectiveness of the Company's policies and business practices which impact on the financial integrity of the Company, including those relating to internal auditing, insurance, accounting, information services and systems and financial controls, management reporting and risk management.

The Executive Committee is narrowly mandated to act as the approving body for expenditures which have been broadly approved by the Board and which are beyond the approval levels of the President and Chief Executive Officer and to perform such functions and exercise such powers specifically delegated to the committee by the Board. It is composed of three directors, one of whom is a full-time officer of the Company, another who is a full-time officer of Westcoast. The Board has determined that a majority of the committee members is unrelated.

The Environment Committee is composed of three directors, one of whom is a full-time officer of the Company. A majority of the committee members are outside and unrelated. This committee is responsible for reviewing and monitoring the environmental policies and activities of the Company on behalf of the Board.

The Compensation Committee is composed of directors who are unrelated. Two of the three members are full-time officers of Westcoast. This committee is generally responsible for recommending to the Board human resources and compensation policies and guidelines for application to the Company and for implementing and overseeing human resources and compensation policies approved by the Board. In addition, it is responsible for periodically reviewing the adequacy and form of the compensation of directors and for ensuring that the compensation realistically reflects the responsibilities and risks involved in being an effective director of the Company and for reporting and making recommendations to the Board accordingly.

The Nominating and Corporate Governance Committee is composed of unrelated directors, a majority of whom, including the Chair, are outside directors. This committee's prime responsibility is for developing and monitoring the Company's overall approach to corporate governance issues and for administering a corporate governance system which is effective in the discharge of the Company's obligations to its shareholders. The nominating responsibility of this committee includes proposing new members to the Board, establishing criteria for Board membership, recommending composition of the Board and its committees, assessing directors' performance on an ongoing basis and developing an orientation and education program for new members of the Board.

Chairman

The Board has determined that the present Chairman of the Company is an outside and unrelated director and independent of management.

Shareholder Feedback and Concerns

In conjunction with the Westcoast investor relations department, the Company maintains an active shareholder relations program. The program is designed to ensure that shareholder inquiries receive a prompt response either from the investor relations department or an appropriate officer of the Company.

Decisions Requiring Board Approval

The Board operates by seeking the advice of and delegating powers, duties and responsibilities to committees of the Board, by delegating certain of its authorities to management and by reserving certain powers to itself. In addition to those matters which must by law be approved by the Board, the Board retains the responsibility for managing its own affairs including selecting its Chair, nominating candidates for election to the Board, constituting committees of the Board and determining director compensation.

Expectations of Management

Members of the management team report to the Board on a regular basis to review the Company's financial and operational results and the Company's progress in fulfilling its strategic goals and objectives. The Committee will be developing processes for defining the Board's expectations of management such as reviews of the Company's strategic plan with management and a comprehensive review of the performance of the President and Chief Executive Officer, which review is carried out by the Compensation Committee.

Concluding Statement

The Company has adopted or is in the process of adopting the recommendations for improved corporate governance established by the TSE.

(Dollar amounts are in thousands except per share and per GJ figures)

For the years ended December 31	1996	1995	1994
DELIVERIES (TJ)*			
Residential	3 056	2 644	2 580
Commercial	2 559	2 217	2 183
Small industrial	2 120	1 905	1 924
Large industrial	30 981	27 890	31 339
Total energy delivered	38 716	34 656	38 026
Customers at year end	27,978	26,638	25,714
AVERAGE RATES PER GJ*			
Residential	$ 4.90	5.30	5.31
Commercial	3.58	4.58	4.65
REVENUE			
Residential	$ 14,971	14,026	13,708
Commercial	9,157	10,161	10,148
Small industrial	3,354	4,013	3,903
Large industrial	33,842	30,237	34,125
Off-system	1,068	2,119	—
Other	431	442	442
	$ 62,823	60,998	62,326
EXPENSES			
Cost of sales	$ 14,975	19,943	22,281
Operating	16,611	16,518	16,527
Interest	8,822	8,915	7,918
Depreciation & amortization	6,792	5,646	4,969
Income taxes	8,238	3,785	4,030
	$ 55,438	54,807	55,725
Net Income	$ 7,385	6,191	6,601
PER COMMON SHARE			
Earnings	$ 2.01	1.67	1.80
Dividends	0.96	0.94	0.88
CAPITALIZATION			
Long term debt	$ 74,862	80,056	63,990
Deferred income taxes	1,863	15,514	15,731
Contributions in aid of construction	10,254	8,799	8,956
Preferred shares	18,910	5,000	5,000
Common equity	54,785	51,038	48,432
Total Capitalization	$ 160,674	160,407	142,109
UTILITY PLANT			
In service (net)	$ 167,249	163,220	154,003
Construction in progress	1,244	1,929	2,590
Total investment in utility plant	$ 168,493	165,149	156,593

1993	1992	1991	1990	1989	1988	1987
2 336	1 510	1 517	1 392	1 259	1 221	1 065
2 102	1 420	1 484	1 518	1 414	1 429	1 300
1 984	1 574	1 518	1 456	1 479	1 400	1 426
31 084	29 592	30 734	30 527	28 283	30 042	30 219
37 506	34 096	35 253	34 893	32 435	34 092	34 010
24,667	17,282	16,042	14,984	13,892	13,061	12,370
5.03	5.15	4.83	4.56	4.50	4.49	4.36
4.36	4.54	4.33	4.17	4.15	4.15	3.99
11,740	7,770	7,321	6,349	5,666	5,476	4,640
9,158	6,443	6,427	6,327	5,862	5,934	5,184
3,665	2,486	3,048	3,985	4,569	4,344	4,672
32,566	32,364	51,202	59,209	57,567	60,309	60,157
—	—	—	—	—	—	—
345	246	299	313	193	194	192
57,474	49,309	68,297	76,183	73,857	76,257	74,845
20,390	17,302	35,886	45,669	44,578	47,375	46,471
16,143	13,096	12,037	11,148	11,223	11,656	10,962
7,781	7,504	7,523	7,709	7,420	7,327	7,402
4,420	4,136	3,805	3,819	3,563	2,919	3,050
2,777	1,868	3,078	2,280	1,924	2,183	2,337
51,511	43,906	62,329	70,625	68,708	71,460	70,222
5,963	5,403	5,968	5,558	5,149	4,797	4,623
1.63	1.48	1.67	1.56	1.44	1.34*	1.30
0.88	0.80	0.78	0.75	0.75	0.75	0.73
67,937	51,875	55,817	42,763	44,937	47,116	49,371
15,703	14,877	14,919	14,919	15,051	14,859	15,643
9,114	3,613	3,728	2,515	2,428	2,459	2,489
5,000	5,000	5,000	5,000	5,000	5,000	5,000
44,787	42,020	39,357	35,983	33,151	30,740	29,795
142,541	117,385	118,821	101,180	100,567	100,174	102,298
144,301	126,612	122,536	119,725	109,509	107,328	101,755
1,789	1,028	1,553	1,108	1,129	584	945
146,090	127,640	124,089	120,833	110,638	107,912	102,700

* TJ refers to Terajoules and is equivalent to 1,000 GJ.

* GJ refers to Gigajoules, a metric unit of energy equivalent to 10^9 joules.

* Before 1988 extraordinary item of $1,049,000 (31 cents per share)

Directors

Robert F. Chase [1]
President and Chief Executive Officer
South Pacific Resources Corp.
Vancouver, British Columbia

Roy G. Dyce [3,4]
President and Chief Executive Officer
Pacific Northern Gas Ltd.
Vancouver, British Columbia

George L. Malpass [5]
President and Chief Executive Officer
Primex Forest Products Ltd.
Delta, British Columbia

Hugh C. Morris [1,2,3]
President
Padre Resources Corporation
Delta, British Columbia

Robert F. O'Shaughnessy [3]
Professional Engineer
Galiano Island, British Columbia

Kenneth E. Rekrutiak [2]
Senior Vice President and
Chief Administrative Officer
Westcoast Energy Inc.
Vancouver, British Columbia

Richard D. Walker [4,5]
Chairman of the Board
Pacific Northern Gas Ltd.
Vancouver, British Columbia

Arthur H. Willms [2,4,5]
President and Chief Operating Officer
Westcoast Energy Inc.
Vancouver, British Columbia

Graham M. Wilson [1]
Executive Vice President and
Chief Financial Officer
Westcoast Energy Inc.
Vancouver, British Columbia

1 Audit Committee
2 Compensation Committee
3 Environment Committee
4 Executive Committee
5 Nominating and Corporate Governance Committee

Officers

R.D. Walker
Chairman of the Board

R.G. Dyce
President and Chief Executive Officer

W.R. Hough
Vice President, Engineering and Operations

T.W. Weaver
Comptroller

D.G. Unruh
Secretary

K.L. Wharton
Assistant Secretary

W.M. Bingham
Treasurer

Head Office

1185 West Georgia Street
Suite 1400
Vancouver BC V6E 4E6

604 691 5680 telephone
604 691 5863 facsimile

Principal Field Operating Office

2900 Kerr Street
Terrace BC V8G 4L9

Registrar and Transfer Agent

Montreal Trust Company
Vancouver, Calgary,
Regina, Winnipeg,
Toronto, Montreal

Auditors

Ernst & Young
Vancouver BC

Annual Meeting

The Annual Meeting of the Shareholders of Pacific Northern Gas Ltd. will be held in the Garibaldi Room at the Four Seasons Hotel, Vancouver, British Columbia, on Wednesday, April 23, 1997 at 10:30 AM (Local Time).

Pacific Northern Gas Ltd.

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